

Privatization of Services

Background

Increasingly, public organizations are utilizing third-party vendors to provide services that are not part of the organization's core business focus. For a number of years, LEAs have frequently contracted with outside service providers to perform support functions such as food service, maintenance and custodial services, transportation, and, more recently, information technology support.

Third-party private vendors now are providing services related directly to instruction and other functions typically considered the core business focus of public schools, including special education services and staff development. During the 1990s, LEAs have contracted with private companies to operate entire schools and school districts, including administration, instruction, and support operations. Such privatization of education presents a new element in the utilization of third-party vendors that does not fit easily into the current accounting framework.

The evolution in the range and scope of services provided by third-party vendors to LEAs has resulted in several new issues related to the accounting of expenditures. LEAs must determine the necessity and most effective method of the following:

- Tracking expenditures for privatized services functionally (e.g., how to account for contractors who provide instructional and administrative services)
- Accounting for expenditures under the appropriate classification codes, including contracts that include both professional services and material goods (e.g., custodial services that include supplies)
- Obtaining detailed information on expenditures from third-party vendors for services rendered

LEAs who utilize third-party vendors to provide major services are challenged by the need to evaluate the cost-effectiveness of utilizing these vendors. It is important that LEAs maintain expenditure data in a form that allows for effective evaluation of costs and benefits, while also recognizing that third-party vendors may be reluctant to provide significant detail on expenditures. Thus, the requirements for third-party vendors to provide detailed expenditure data to LEAs is essentially a local governance and contracting issue.

LEAs should be encouraged to obtain and report detailed expenditure data from third-party vendors who provide educational services, where appropriate and obtainable. Generally, these requirements should be included in service contracts with vendors with enforceable information access provisions. The administrative costs to both the vendor and the LEA should be prime considerations in determining the types and quantities of financial, student and other performance data from vendors.

The current Handbook contains a number of expenditure object codes that may be utilized by LEAs to capture the costs associated with services provided by third party vendors. Expenditure object codes in the 300 series (Purchased Professional and Technical Services), 400 series (Purchased Property Services) and 500 series (Other Purchased Services) may be utilized for these purposes. The expenditure object codes should be used in conjunction with the appropriate function code based on the purpose of the services being purchased. However, these codes do not provide LEAs with the ability to account for vendor costs at a detailed level

Accounting Treatment

In order to allow LEAs to track and report vendor expenses at a detailed level (e.g., salaries, materials, etc.), additional detailed expenditure sub-object codes are required in a number of the existing expenditure object codes. The additional detailed expenditure sub-object codes will provide the ability of LEAs to track vendor expenses where appropriate.

Proposed Handbook Revision

We recommend that the Handbook be revised to include as short paragraph related to the reporting of detailed vendor expenses within expenditure sub-object codes in the 300 series of expenditure object codes. This paragraph should follow the definition of the expenditure object code.

“An LEA may (at its discretion) record and report an additional level of detail related to expenditures made for services provided by professional or technical firms. In order to record and report detailed expenditures in this area, an LEA should utilize the following structure and categories within the 300 object or the 310, 320, 330 or 340 sub-object codes.

3X1 Vendor Salaries, Wages and Benefits

3X2 Vendor Professional and Contracted Services

3X3 Vendor Supplies and Materials

3X4 Vendor Other Operating Costs

3X5 Vendor Debt Costs

3X6 Vendor Capital Costs

3X7 Vendor Fee (Revenue less Total Expenses)

In order to record and report such detail, an LEA would have to receive detailed reporting of these costs from an external service firm.”

Coding Examples

1. An LEA enters into a contract with a third party vendor to provide instructional services to learning disabled students. The expenditures for the contract total \$500,000, and the contract does not require detailed financial reporting of expenditures from the vendor (other than those for state and federal compliance purposes).

The costs of \$500,000 associated with the contract should be coded to program code 240 (Learning Disabled) utilizing expenditure object code 320 (Professional – Educational Services) and function code 1000 (Instruction).

2. An LEA contracts with an external medical services firm to provide nursing services to its elementary students. The LEA enters an annual contract with the firm for which it pays a flat fee of \$120,000 annually regardless of usage levels. The contract does not require detailed reporting of expenditures by the medical services firm; however, the firm assists the LEA in the preparation and submission of information for the reimbursement from federal sources for Medicaid-eligible costs.

The costs of \$120,000 associated with the contract should be coded to program code 000 (Undistributed Expenditures) utilizing expenditure object code 330 (Other Professional Services) and function code 2134 (Nursing Services).

3. An LEA enters into a contract with a third party vendor to provide instructional services to learning disabled students. The expenditures for the contract total \$500,000, and the contract requires detailed financial reporting of expenditures from the vendor. The vendor reports the following expenditures to the LEA:

- \$300,000 for salaries to instructional personnel
- \$50,000 for benefits for instructional personnel
- \$40,000 for direct purchased supplies
- \$10,000 for direct purchased maintenance services
- \$50,000 for utilities
- \$25,000 in allocated administrative costs
- \$25,000 in vendor profits

Based on the detailed cost information provided by the vendor, the LEA may code the \$500,000 expenditure in the following manner:

- \$350,000 for salaries to expenditure object code 321 (Professional Educational Services – Vendor Salaries, Wages and Benefits); program code 240 (Learning Disabled) utilizing function code 1000 (Instruction)
- \$40,000 for direct purchased supplies to expenditure object code 323 (Professional Education Services – Vendor Supplies and Materials); program code 240 (Learning Disabled) utilizing function code 1000 (Instruction)
- \$10,000 for direct purchased maintenance services to expenditure object code 322 (Professional Education Services – Vendor Professional and Contracted Services); program code 240 (Learning Disabled) utilizing function code 1000 (Instruction)
- \$50,000 for utilities to expenditure object code 323 (Professional Education Services – Vendor Other Operating Costs); program code 240 (Learning Disabled) utilizing function code 1000 (Instruction)
- \$25,000 in allocated administrative costs to expenditure object code 327 (Professional Education Services – Vendor Fee); program code 240 (Learning Disabled) utilizing function code 1000 (Instruction)
- \$25,000 in vendor profits to expenditure object code 327 (Professional Education Services – Vendor Fee); program code 240 (Learning Disabled) utilizing function code 1000 (Instruction)